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No. 92-1839

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

COLGATE-PALMOLIVE COMPANY,
Petitioner,

v.

FRANCHISE TAX BOARD,
An Agency of the State of California,
Respondent.

On Writ of Certiorari to the Court of Appeal of the State of California in and for the Third Appellate District

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REPLY BRIEF OF PETITIONER

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REPLY BRIEF OF PETITIONER

INTRODUCTION

The central question in this case is whether worldwide combined reporting as applied to a U.S.-based multinational group frustrates federal foreign policy in violation of the Foreign Commerce Clause. Up to this juncture, the dispute over this question has focused on its substance—whether worldwide combined reporting offends federal foreign policy and, if so, whether that policy has been expressed with sufficient clarity to preclude California from requiring Colgate to report on a worldwide combined basis. Now, however, the Solicitor General has filed an *amicus* brief which attempts to direct the Court's focus away from the federal opposition to California's method.

Contrary to the position that the United States has previously taken in this case (*see* Pet. Br. 34-38),[1] the Solicitor General has pledged a new-found allegiance to respondent. The Solicitor General's about-face is based not on his view of the merits of Colgate's claim, but rather on his view that, in determining whether worldwide combined reporting violates the Foreign Commerce Clause, the appropriate inquiry is whether there was an articulated federal policy in effect during 1970-73, the tax years here at issue. Since such policy was allegedly unclear in 1970-73, Colgate's claim, in the Solicitor General's view, must fail. Undertaken without reference to any authority in the prior decisions of this Court, the Solicitor General's eleventh-hour repudiation of the long-standing views of the United States cannot be justified in terms of the legal principles that have governed—and that should continue to govern—dormant Foreign Commerce Clause analysis.

In addition, both the Solicitor General and respondent contend that, even if a decision is rendered in favor of Colgate, relief should be granted on a prospective-only basis. The contention is wholly without merit. Not only

[1] References to the Brief of Petitioner are denominated "Pet. Br." followed by a page reference.

is respondent procedurally barred from raising this issue before the Court, but this Court's precedents also dictate that Colgate be granted relief on a retroactive basis. Finally, neither the Solicitor General nor respondent has persuasively challenged the arguments raised by Colgate in its opening brief.

I. THE CONSTITUTIONALITY OF WORLDWIDE COMBINED REPORTING UNDER THE FOREIGN COMMERCE CLAUSE MUST BE EVALUATED IN LIGHT OF THE OVERALL EVIDENCE OF THE NATION'S FOREIGN POLICY, REGARDLESS OF THE TAX YEARS AT ISSUE

The Solicitor General, speaking for the United States, has put to rest any question whether federal policy is opposed to worldwide combined reporting: "In the present dispute, it is quite clear that federal law has long embodied a preference for the arm's length method . . .," SG Br. 17 (emphasis omitted),[2] and that "the executive branch since 1982 has opposed the States' application of WWCR to domestic as well as foreign corporations," *id.* at 26. Nor does the Solicitor General deny that such policy has been expressed with sufficient clarity to bar states from requiring taxpayers to report on a worldwide combined basis.[3] Rather, the Solicitor General's support of respondent in this case is explained largely by the fact that, in his view, Colgate sued *for the wrong tax years.*[4]

[2] Citations to the Brief for the United States as *Amicus Curiae* Supporting Respondent, filed by the Solicitor General in this case and in *Barclays*, will be referred to throughout this brief as "SG Br." followed by a page reference.

[3] While the Solicitor General purports to refrain from expressing the United States' view as to the compatibility of worldwide combined reporting with federal foreign policy (SG Br. 23 n.16), he acknowledges that the United States, in its prior briefs, has consistently taken the position that the Foreign Commerce Clause bars the states from requiring worldwide combined reporting because it is "contrary to the federal government's foreign commercial policy." SG Br. 21.

[4] To be sure, the Solicitor General also suggests that Colgate's claim fails because the Federal Government has not expressed its opposition to worldwide combined reporting as applied to a domestic-based taxpayer in terms of foreign policy. However, as discussed below (*see infra*, pp. 19-20), the Solicitor General's argument is without merit.

According to the Solicitor General, if only Colgate had sought relief for the tax years during which such federal foreign policy had become manifest, Colgate would have had a substantial claim. However, since such policy allegedly was unclear in 1970-73—the tax years here at issue—Colgate's claim, according to the Solicitor General, must fail.

As we demonstrate below, a coherent approach to the Foreign Commerce Clause question raised by this case requires that the constitutionality of worldwide combined reporting be evaluated in terms of the overall evidence of the nation's foreign policy regarding the method of taxation at issue, regardless of the particular tax years involved and regardless of the fact that the state has prospectively changed its taxing method.[5] On not one occasion has this Court ever looked to the year a tax accrued to determine the Federal Government's policy in analyzing the "one voice" test. Rather, this Court has uniformly looked to all of the evidence in the record before it of the policy of the Federal Government with respect to the method of taxation at issue. Moreover, the approach suggested by the Solicitor General would create an utterly illogical standard for adjudicating future controversies that would serve to undermine the very purpose of the Foreign Commerce Clause.

Finally, even if the Court were to adopt the Solicitor General's views as to the proper approach to this case, the record supports the conclusion that federal policy

[5] It is still unclear when the change in California law allegedly easing the burdens of worldwide combined reporting will finally take place. As enacted in September 1993, the effective date of S.B. 671 was January 1, 1994. However, legislation pending in California will delay the effective date of S.B. 671 to as late as November 30, 1994, for certain fiscal-year taxpayers. Cal. A.B. 791, 1993-94 Reg. Sess. (Jan. 27, 1994) § 3.

opposing worldwide combined reporting had been established by the years at issue here.

A. In Analyzing Whether a State Tax Violates the "One Voice" Test, Both This Court and the United States Have Consistently Looked to the Federal Government's Complete Course of Conduct as Evidence of Foreign Policy

In determining whether a state tax violates the "one voice" criterion of the Foreign Commerce Clause—because it "*either* implicates foreign policy issues which must be left to the Federal Government *or* violates a clear federal directive" (*Container*, 463 U.S. at 194 (emphasis in original))—the Court has always evaluated the constitutionality of the state tax in light of all of the evidence in the record regarding the foreign policy of the Federal Government. Thus, in *Japan Line*, the source of the Court's contemporary Foreign Commerce Clause doctrine limiting state taxing power, the Court examined the impact that California's tax had on the Federal Government's ability to "speak with one voice" in the years leading up to 1978, the date of the Court's decision, not as of 1970-72, the tax years at issue. *Japan Line*, 441 U.S. at 452-53 & nn.17-18.

Similarly, the Court in *Container* did not limit its "one voice" analysis to statements of the Federal Government made during 1963-65, the tax years at issue in that case. Rather, the Court looked for, but could not find in the record then before it, evidence of a course of foreign policy that indicated whether California's tax created an unconstitutional interference. *See Container*, 463 U.S. at 195-96. More recently, in *Itel*, the issue before this Court was the validity of a state tax affecting cargo containers used in international trade. The petitioner argued that in *Japan Line* the Federal Government had interpreted a 1956 Container Convention as prohibiting all domestic taxes on international cargo containers. However, this Court rejected the petitioner's argument and looked to later indications of the federal government's foreign policy. *Itel*, 113 S. Ct. at 1101. *See also*

Kraft, 112 S. Ct. at 2370-71 (same); *Wardair*, 477 U.S. at 9 (same).[6]

Like the Court, the United States—at least prior to the filing of its *amicus* brief here—has always looked to the overall evidence of the Federal Government's foreign policy in apprising the Court of its views on whether particular state taxes at issue preclude the Federal Government from "speaking with one voice." Thus in his *amicus* briefs filed in *Japan Line, Chicago Bridge & Iron Co. v. Caterpillar Tractor Co.*, 463 U.S. 1220 (1983), *Wardair*, and *Kraft*, the Solicitor General has consistently focused on the Federal Government's existing foreign policy as it has developed over the years—not just the foreign policy that may have been in effect during the tax years at issue—in analyzing the question whether the tax before the Court prevented the Federal Government from "speaking with one voice."[7] In addition, the Solicitor General in each of these prior briefs has relied upon the actions and statements of federal officials to establish the Federal Government's policy, as opposed to simply presuming that the most recent *amicus* brief itself establishes policy. *See supra*, n.7.

The Solicitor General argues that federal policy must be determined at the time a tax accrues because no

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[6] Prior decisions regarding the date as of which the law or federal government policy should be determined uniformly follow the rule of decision established almost two centuries ago in *United States v. Schooner Peggy*, 5 U.S. (1 Cranch) 103 (1801). Chief Justice Marshall explained that "in great national concerns" the Court must decide cases "according to existing laws," even if the laws intervene after a judgment and before decision on appeal. *Id.* at 110. This Court has consistently applied that rule whether the law at issue has been constitutional, statutory, judicial, or new policy of an executive department. *Thorpe v. Housing Authority*, 393 U.S. 268, 281-82 (1969).

[7] *See* Brief for the United States as *Amicus Curiae* at 13, 20-26, 28-30, *Japan Line* (No. 77-1378); Brief for the United States as *Amicus Curiae* at 2-3, 14, 16-17, *Chicago Bridge* (No. 81-349); Brief for the United States as *Amicus Curiae* at 3-30, 34-36, *Wardair* (No. 84-902) (Lexis); Brief for the United States as *Amicus Curiae* at 22, *Kraft* (No. 90-1918).

amount of creativity can overcome the overwhelming evidence in the record of a clear federal directive condemning the state method of taxation at issue here. Colgate has catalogued the unbroken stream of federal statements and actions opposing worldwide combined reporting as applied to both domestic and foreign corporations (Pet. Br. 34-38), the existence of which the Solicitor General himself is forced to concede (SG Br. 26). While the Solicitor General, for whatever reason, urges a *result* sustaining the tax, he cannot alone (nor does he attempt to) set a new policy regarding the method of taxation applied to Colgate for the 1970-73 tax years.[8] Quite simply, the Federal Government's policy toward worldwide combined reporting is evidenced by the entire federal course of conduct contained in the record before the Court. That entire course of conduct condemns application of worldwide combined reporting, as it existed prior to California's eleventh-hour revision of the method, to Colgate for the 1970-73 tax years before this Court.

B. The Solicitor General's Approach to the Issues in This Case Ignores Practical Realities and Will Serve to Undermine the Very Purpose of the Foreign Commerce Clause

The Solicitor General, in an extraordinary last-minute turnaround, has sought to distance himself from the approach he has taken in his earlier submissions, boldly asserting that "[o]ur prior briefs in this case were flawed." SG Br. 21. It is, however, the Solicitor General's newly concocted approach to the Foreign Commerce Clause, not the approach that he and the Court have taken in prior cases, that is "flawed." In fact, the established approach makes good sense and good law.

The appropriate time for determining the Federal Government's foreign policy should reflect the purpose of the constitutional requirement barring taxes that impair the

[8] In fact, given California's revision of the tax method at issue here, there is no need for the Federal Government to readdress its long-established policy.

ability of the Federal Government to "speak with one voice." Simply put, that purpose is to avoid embarrassment of the Federal Government in the conduct of its foreign commercial policy. The critical moment for determining when the Federal Government may be embarrassed by state taxes that undermine its foreign policy is the moment when those taxes have their economic "bite." It is at this moment that the levy's impact is felt most acutely. Consequently, the most logical time for ascertaining whether a tax frustrates federal foreign policy is the moment when the tax is definitively enforced by the state taxing authority, through judicial proceedings if necessary, not when the tax technically accrues under state law.

This straightforward reasoning underlies existing law and practice which looks to the time when a tax is definitively enforced as the proper time for determining whether the tax impairs the ability of the Federal Government to "speak with one voice." In contrast, the Solicitor General's suggestion that the Court look to foreign policy at the time a tax accrues would not only constitute a radical departure from the sound approach the Court and the Solicitor General have previously embraced, it would also lead to absurd results that would disserve the underlying purposes of the Foreign Commerce Clause.

Assume, for example, that a state tax affecting foreign commerce accrues during year 1, before the Federal Government has had a reasonable opportunity to evaluate the impact of the levy on federal foreign commercial policy. Assume further that the taxpayer challenges the constitutionality of the tax in year 2, informing the Federal Government of the taxpayer's view that the tax frustrates foreign policy. Finally, assume that over the next five years, as the case makes its way through the administrative and judicial process, the Federal Government articulates the firm opinion that imposition of the levy is incompatible with the conduct of federal foreign commercial policy. Under the Solicitor General's approach, if the state sought to enforce the tax in year 7, after judicial proceedings were complete and after the Federal Government had

firmly concluded that imposition of the tax frustrated federal foreign policy, the tax would nevertheless be sustained because the policy had not been clearly established in year 1 when the tax accrued.

The Solicitor General's approach cannot be squared with the purposes of the Foreign Commerce Clause. Plainly, the purposes of the Foreign Commerce Clause, as reflected in the "one voice" test, would be undermined by an approach that required the Court to ignore the total impact that imposition of a state tax has on federal foreign policy and to rest its judgment instead on a purely historical inquiry. It would indeed be perverse if the Foreign Commerce Clause were construed to sanction taxes whose existing application frustrates federal policy, merely because at some earlier time federal policy regarding such taxes had not been clearly articulated, while condemning taxes whose application is wholly consonant with federal policy, merely because at some earlier time federal hostility to such taxes had been clearly expressed.

Moreover, the Solicitor General's approach ignores economic, political, and diplomatic realities. As a practical matter, in many (if not in most) instances, it will take a number of years after a tax accrues for taxpayers and the Federal Government to determine whether, and the extent to which, state taxes concretely frustrate federal foreign policy. There is, in effect, a natural gestation period during which taxpayers assess the precise effect of a state tax upon their conduct of foreign commerce and the Federal Government assesses the impact of the tax upon its foreign policy concerns. To measure the compatibility of a state tax with the nation's foreign policy at the time of the tax's accrual rather than the time of its definitive enforcement would thus result in a constitutional mismatching of gross proportions.

C. A Federal Policy Opposing Worldwide Combined Reporting Had Been Established by the Tax Years at Issue

Finally, even assuming *arguendo* that the time for determining whether a state tax violates the "one voice" standard is when the tax accrues, Colgate must nevertheless prevail because federal policy opposing worldwide combined reporting had been established by the tax years at issue. The Solicitor General's argument to the contrary was evidently formulated without regard to the record in this case, or federal actions for tax years before 1982.

The record in this case is undisputed that, as of 1970-73, the Federal Government had a policy opposing states' use of worldwide combined reporting. The trial court made a specific finding to this effect, based on statements of the Federal Government relevant to the 1970-73 time period. Pet. App. F at 100a-02a. Hence even under the Solicitor General's approach to this case, California is barred from applying worldwide combined reporting to Colgate.

Moreover, the United States' own actions cannot be reconciled with the Solicitor General's newly adopted position that, prior to the 1980s, there was no federal policy opposing worldwide combined reporting. The United States in fact received a settlement payment on the basis that worldwide combined reporting was unconstitutional for the period 1975-78. *United States v. Alaska*, No. A87-328 (D. Alaska filed July 15, 1987).[9] It is un-

[9] That suit related to an increase in the Alaska tax burden of Husky Oil Company and a subsidiary. The United States was obligated to pay this increase under a cost-plus contract. Thus, the Solicitor General displays substantial unfamiliarity with the long-standing controversy over other states' use of worldwide combined reporting when he asserts that the United States is "not aware of any objections expressed by the affected taxpayers" in Alaska or Tennessee (SG Br. 28 n.22). The Department of Justice, which brought the Alaska suit on behalf of the United States, was certainly aware of disputes in Alaska. Indeed, there are a number of

seemly, to say the least, for the Federal Government to be repudiating a position on which it has relied to extract a monetary settlement from a sovereign state.

II. IF COLGATE PREVAILS IN THIS CASE, RELIEF MUST BE GRANTED ON A RETROACTIVE BASIS

A. Respondent Is Barred by State Law from Raising the Issue of Prospectivity

Respondent asks this Court to "apply any decision regarding the validity of WWCR prospectively only." Resp. Br. 42. Respondent raised the prospectivity issue *for the first time* at oral argument before the California Court of Appeal. Under California law, an issue raised for the first time in oral argument is deemed waived. *See, e.g., Kinney v. Vaccari*, 27 Cal. 3d 348, 356-57 n.6, 612 P.2d 877, 881 n.6, 165 Cal. Rptr. 787, 791 n.6 (1980); *Chatterjee v. Kizer*, 231 Cal. App. 3d 1348, 1366 n.4, 283 Cal. Rptr. 60, 70 n.4 (2d Dist. 1991); *Estate of Davis*, 38 Cal. App. 2d 579, 587, 102 P.2d 545, 545 (1st Dist. 1940). The California Court of Appeal therefore refused to entertain this issue at oral argument. *See* extracts from transcript of oral argument before the Court of Appeal reproduced in App. A.

This Court has held that it does not have jurisdiction over a federal question unless that question has been raised and pursued in a timely manner in state court proceedings. *See Michel v. Louisiana*, 350 U.S. 91, 97 (1955); *Williams v. Georgia*, 349 U.S. 375, 382-83 (1955). *See also Hulbert v. Chicago*, 202 U.S. 275 (1906); *Stembridge v. Georgia*, 343 U.S. 541, 547 (1952). "It is clear that this Court is without power to decide whether constitutional rights have been violated when the federal questions are not seasonably raised in accordance with the requirements of state law." *Edelman v. California*, 344 U.S. 357, 358 (1953). Because respondent has failed to raise the question of prospectivity

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other "affected taxpayers" who have expressed similar objections. *See Amicus Curiae* Brief on Behalf of the States of Alaska *et al.* (No. 92-1839) at 2, n.5.

in a timely manner in the state court proceedings, it is barred from raising the question before this Court.

B. Respondent Is Barred by Contractual Obligation from Raising the Issue of Prospectivity

Respondent is contractually bound to apply relief in this case on a retroactive basis. The precise language of the stipulation that respondent and Colgate entered into states that Colgate would be entitled to refunds if it was ultimately determined that respondent may not combine Colgate with its foreign subsidiaries in a single, worldwide group. *See* J.A. 6. California law is clear that a stipulation of counsel "must be construed by an *objective standard*" (*Consolidated Dock & Storage Co. v. Superior Court of L.A. County*, 18 Cal. App. 3d 949, 952, 96 Cal. Rptr. 254 (2d Dist. 1971) (emphaiss supplied)) and that "[i]t is immaterial that one of the parties had an undisclosed intention or belief as to what it meant" (*id.*). Respondent's previously-undisclosed belief that the stipulation "provides a computation only" (Resp. Br. 43 n.12) is contradicted by the plain language of that agreement which state law requires must govern. "It is up to the parties to state a stipulation clearly and properly if they intend to be bound by it . . . ." *Bemer v. Bemer*, 152 Cal. App. 2d 766, 771-72, 314 P.2d 114 (2d Dist. 1957).

Moreover, respondent's claim that it was entitled to raise *any* question of law on appeal, whatever the language in the stipulation, is belied by the well-established role of a stipulation in *narrowing* the issues to be tried. *Id.* at 771. Indeed, it was precisely because it was the subject of the stipulation that the parties did *not* try the issue regarding the amount of the refund to which Colgate was entitled.

C. Assuming *Arguendo* That the Prospectivity Issue Is Properly Before This Court, Respondent Has Presented No Valid Reason Why the Court's Ruling in *Harper* Requiring Retroactivity Should Not Be Applied in This Case

Even assuming that the prospectivity issue which respondent seeks to raise is properly before this Court, re-

spondent's argument utterly fails to demonstrate why the "'normal rule of retroactive application'" (*Harper v. Virginia Dep't of Taxation*, 113 S. Ct. 2510, 2518 (1993) (quoting *James B. Beam Distilling Co. v. Georgia*, 111 S. Ct. 2439, 2445 (1991))) should not apply in this case. Indeed, respondent's discussion of prospectivity reflects a profound confusion over the issues that bear on the merits of this case—issues that are irrelevant to the prospectivity issue—and those that bear on Colgate's entitlement to "meaningful backward-looking relief" (*McKesson Corp. v. Division of Alcoholic Beverages & Tobacco*, 496 U.S. 18, 31 (1990)), assuming it prevails on the merits. Colgate nevertheless addresses arguments that respondent raises under the rubric of "prospectivity" (Resp. Br. 42-49), even though some of them do not logically belong there.

First, respondent argues that, "[u]nder *Harper*, *Container* is controlling as to Colgate's claim for relief." Resp. Br. 43. Colgate agrees. *Harper* holds that when a rule of law has been applied to parties before the Court, that rule of law generally must be applied retroactively. Accordingly, the rule of law embodied in *Container* controls the outcome of this case. As Colgate has explained at length in its opening brief, however, the rule of law embodied in *Container*, viewed in light of the clear evidence of the Federal Government's opposition to worldwide combined reporting, requires that judgment be rendered in favor of Colgate. In short, there is no issue in this case about the prospective or retroactive application of *Container*.[10]

[10] Similarly, confusion is evident in respondent's suggestion that retroactive relief should not be awarded "under *Harper*" because this case involves "a species of 'transient' unconstitutionality" that arises from "the interaction of [worldwide combined reporting] with independent events that exist within a particular time frame." Resp. Br. 45. Because these events did not occur until after 1973, respondent argues, "Colgate should be denied relief and the question of retrospective operation should be reserved." Resp. Br. 46. Again, respondent has confused the substantive issue in this case with the question of prospectivity. In order to reach a decision on the merits in Colgate's favor, the Court must find that worldwide combined reporting has been unconstitutionally imposed upon Colgate. It is at that stage of the analysis that the question whether —and when—there was a federal foreign policy in place has a bearing on Colgate's claim. Once a determination of unconstitutionality has been made, however, the timing of the events that led to that determination has no bearing on the question whether that determination should be applied prospectively. *See infra* pp. 14-17.

Second, in its discussion of "prospectivity" respondent argues against overturning *Container* on *stare decisis* grounds in light of the fact that Congress is free to act in this area.[11] This argument is, of course, inapposite. Colgate has not suggested that this Court overturn *Container*. Rather, Colgate is asking this Court to apply *Container* to the factual record before it. *See supra* p. 12. Furthermore, respondent may have asked for too much. As this Court found in *Japan Line* when the County of Los Angeles raised a similar argument, "to say that California has created a problem susceptible only of congressional . . . solution is to concede that the taxation [at issue] is an area where a uniform federal rule is essential." *Japan Line*, 441 U.S. at 454.

Far from precluding relief, the Court strongly indicated in *Harper* that its decisions must be applied on a retroactive basis in all instances. To be sure, the Court in *Harper* was able to rest its decision on the narrower ground that any rule of law applied to the parties before the Court must be applied retroactively to other cases on direct review. Nevertheless, the Court's references in *Harper* to its lack of "constitutional authority . . . to disregard current law'" (*id.* at 2517 (quoting *American Trucking Ass'ns v. Smith*, 496 U.S. 167, 214 (1990) (Stevens, J., dissenting))) and the fundamental rule of "'retrospective operation'" (*id.* at 2516 (quoting *Kuhn*

[11] The fact that respondent raises this argument in the context of its discussion of prospectivity is ironic in light of Justice Scalia's recent statement that "[p]rospective decisionmaking is the handmaid of judicial activism, and the born enemy of *stare decisis*." *Harper*, 113 S. Ct. at 2522 (Scalia, J., concurring).

v. Fairmont Coal Co., 215 U.S. 349, 372 (1910) (Holmes, J., dissenting))), as well as its heavy reliance on *Griffith v. Kentucky*, 479 U.S. 314 (1987), requiring retroactive application of its decisions in criminal cases, leave little doubt that retroactive application of its decisions is constitutionally required in all cases. *Accord*, SG Br. 22.

D. Pursuant to *Chevron Oil*, Relief in This Case Must Be Granted on a Retroactive Basis

Both respondent and its *amici* [12] argue that any decision in favor of Colgate in this case should be applied on a prospective-only basis pursuant to the three-part test established by this Court in *Chevron Oil v. Huson*, 404 U.S. 97 (1971). This Court's decision in *Chevron Oil*, however, mandates that the decision herein be applied retroactively.

In *Chevron Oil*, this Court established the now familiar three-part test for determining the limited circumstances in which a party should be granted relief on a prospective-only basis. First, "the decision to be applied nonretroactively must establish a new principle of law, either by overruling clear past precedent on which litigants may have relied . . . or by deciding an issue of first impression whose resolution was not clearly foreshadowed." *Chevron Oil*, 404 U.S. at 106. Respondent argues that a decision in favor of Colgate in this case would require that this Court overrule *Container*, thereby abandoning clear past precedent. Such a suggestion is, of course, absurd. Far from requesting that this Court overrule *Container*, Colgate is in fact relying on the principles established in *Container* as the very cornerstone of its argument. Accordingly, a decision in favor of Colgate in this case would fail to meet the first criterion of the *Chevron Oil* test.

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[12] *See Amicus Curiae* Brief on Behalf of the States of Alaska, *et al.* (No. 92-1839); Brief of *Amicus Curiae* Litton Industries, Inc. *et al.*

The second part of the *Chevron Oil* test, which the Court need not address here,[13] requires that the Court "weigh the merits and demerits in each case by looking to the prior history of the rule in question, its purpose and effect, and whether retroactive operation will further or retard its operation." *Chevron Oil*, 404 U.S. at 106-07. Respondent argues that the changes adopted by California to its worldwide combined reporting statutory scheme "have largely removed the continuing effects of any decision in this case." Resp. Br. 47. In making this argument, respondent ignores the fact that the central issue in this case has considerable continuing implications for a multitude of taxpayers and involves billions of dollars in tax liabilities, not only in California but also in other states. *See Amicus Curiae* Brief on Behalf of the States of Alaska, *et al.*[14] More importantly, the fact that the state had changed its law for the future did not affect this Court's view in *McKesson* that the state must provide "a meaningful opportunity to secure postpayment relief for taxes already paid pursuant to a tax scheme ultimately found unconstitutional." *McKesson*, 496 U.S. at 22.

The third part of the *Chevron Oil* test requires the Court to "weig[h] the inequity imposed by retroactive application" in order to avoid "'injustice or hardship'." *Chevron Oil*, 404 U.S. at 107. Respondent claims that it justifiably relied on this Court's decision in *Container* and retrospective application of an adverse decision would have a significant fiscal impact. Resp. Br. 48. In fact,

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[13] Inquiry into this part (and the third part) of the *Chevron Oil* test is obviated here because the threshold requirement of "overruling" or "novelty" is not satisfied. *Ashland Oil, Inc. v. Caryl*, 497 U.S. 916, 918 (1990).

[14] Moreover, even the Solicitor General has recognized that there is no guarantee that California's new legislation will remedy the past foreign policy interference. His brief at an earlier stage of these proceedings recognizes that issues "might arise in connection with enforcement of the State's new legislation." Brief for the United States as *Amicus Curiae* at 10, *Barclays Bank* (No. 92-1384).

respondent has been well aware of the change in circumstances that has occurred since the *Container* decision, including the clarification of the Federal Government's position on this issue. This, in and of itself, has given the state ample notice that its taxing scheme was in jeopardy and its reliance on *Container* unfounded.[15]

Moreover, this Court has never required that a state *know* of the unconstitutionality of its taxing scheme in order for relief from the imposition of such a scheme to be granted on a retroactive basis. As this Court stated in *Harper*, "the federal law applicable to a particular case does not turn on 'whether [litigants] actually relied on [an] old rule [or] how they would suffer from a retroactive application' of [a] new one." *Harper*, 113 S. Ct. at 2516 (quoting *Beam*, 111 S. Ct. at 2447). In short, *Chevron Oil* requires that this Court balance the equities at issue in this case and, in so doing, there is no precedent to suggest that the financial interests of a state should trump those of a taxpayer with respect to funds that a state has collected unlawfully.

Finally, both respondent and the Solicitor General argue that a violation of the "one voice" test is not the type of constitutional violation that merits retroactive relief. *See* Resp. Br. 48-49; SG Br. 28-30. However, this Court has clearly held that " 'the Due Process Clause of the Fourteenth Amendment obligates the State to provide meaningful backward-looking relief to rectify *any* unconstitutional deprivation.' " *Harper*, 113 S. Ct. at 2519 (quoting *McKesson*, 496 U.S. at 31) (emphasis supplied). Moreover, backward-looking relief is the only way in which the Constitution can discourage states from interfering in foreign policy matters. To limit relief to the

[15] Indeed, contrary to respondent's claim, the state has demonstrated its own doubts regarding the holding in *Container*. *See* Cal. Code Regs. tit. 18, § 25111(i)(5)(B)(i)(II) (1993) (regulation proposed in 1988, and final in 1989, to the effect that a water's-edge election may be revoked retroactively and election fee refunded upon "[a] final appellate level determination that application of the worldwide combined report method is *per se* unconstitutional").

future alone would encourage states to act with total disregard for federal foreign policy, secure in the knowledge that they could recede at the last possible moment and incur no adverse consequences.

III. NEITHER RESPONDENT NOR ITS *AMICI* HAVE RAISED ANY MEANINGFUL CHALLENGE TO THE ISSUES RAISED BY COLGATE IN ITS OPENING BRIEF THAT ARE AT THE HEART OF THIS CASE

Respondent has wholly failed to rebut Colgate's argument that Congress has not consented to worldwide combined reporting. Even the Solicitor General, who supports respondent in this case, finds himself unable to swallow respondent's position on congressional consent. SG Br. 16 n.10. There is simply no basis in this record for concluding that the exacting standard for finding congressional consent to state laws has been met—a standard "requiring that Congress 'manifest its unambiguous intent before a federal statute will be read to permit' state regulation" that would otherwise violate constitutional norms. *Northwest Airlines, Inc. v. County of Kent*, 62 U.S.L.W. 4103, 4108 n.19 (U.S. Jan. 24, 1994) (quoting *Wyoming v. Oklahoma*, 112 S. Ct. 789, 802 (1992)).

Respondent similarly fails to offer any meaningful response to Colgate's argument that the Foreign Commerce Clause demands equal treatment of U.S.-based and foreign-based multinational groups. Rather, respondent attempts to avoid the issue, arguing here for the first time that it was not properly raised in Colgate's claims for refund and therefore is not properly before this Court. Such an assertion is simply wrong. Colgate's claims for refund stated that "application of worldwide unitary combination to the [Colgate] group fails to meet constitutional standards under the due process and equal protection clauses of the United States and California Constitutions and the commerce clause of the United States Constitution." *See* Colgate claims for refund, Joint Exhibits 7a, 7b, 7c, and 7d at 11. This general statement clearly incorporates Colgate's equal-treatment argument. Respond-

ent also raises this argument with regard to the "competitive balance" issue, and the argument similarly fails.

Respondent argues, in addition, that "competitive balance" does not implicate foreign policy and therefore does not raise Foreign Commerce Clause concerns. Resp. Br. 27. In making this argument, however, respondent ignores the clear statements to the contrary cited in Colgate's opening brief, including the statement of the Secretary of State that issues of "competitive balance" are "an integral and important element of overall foreign policy." *See* Pet. Br. 43. Respondent also ignores the trial court's finding, based on the federal statements before it, that "[i]n our case, California's application of the unitary method of taxation . . . conflicts directly with the foreign policy of the federal government . . . ." Pet. App. F at 88a.

Respondent nevertheless asserts that "competitive balance" does not implicate typical "one voice" concerns such as "foreign retaliation" and "disputes over reconciling formulae." Resp. Br. 27. Contrary to respondent's assertions, however, the issue of "competitive balance" is one that has profound implications under the "one voice" test. The very purpose of the "one voice" test is to enable the Federal Government to present a uniform and coherent policy to foreign nations. *See Japan Line*, 441 U.S. at 448-49. It has been a consistent policy of the United States, both in its treaty negotiations and in its other dealings with foreign nations, to ensure a level-playing field for U.S.-based companies. It is hard to imagine a situation more destructive of the credibility of the United States in its quest to enforce this policy than to allow a renegade state's taxing scheme to disregard the concept of "competitive balance."

Respondent's *amici* add little to respondent's unsuccessful efforts to address Colgate's claims on the merits. Indeed, the Solicitor General's analysis of Colgate's "equal treatment" argument demonstrates his lack of familiarity

with, and profound misunderstanding of, the issues that are at the heart of this case. The Solicitor General analyzes Colgate's equal-treatment argument on the premise that Colgate is asserting a constitutional right to equal treatment of *foreign* and *domestic* commerce. He baldly asserts that "that cannot be the law," SG Br. 27 n.21, declaring that "the whole point of *Japan Line* is that taxing practices that are permissible with respect to domestic commerce are sometimes unlawful as applied to foreign commerce and/or foreign taxpayers." In fact, the "whole point"—and one that the Solicitor General has missed entirely—is that, insofar as here relevant, Colgate is not asserting the right to equal treatment of any *domestic* commerce in which it is engaged. Rather, the current issue of the constitutionality of worldwide combined reporting arises entirely out of Colgate's *foreign* commerce (*Container*, 463 U.S. at 188-89), and it is in connection with this foreign commerce that Colgate raises the issue whether the Commerce Clause forbids the states from preferring one form of "foreign" commerce over another.

This fundamental confusion over the nature of Colgate's business may well be responsible for the Solicitor General's unfounded assertion that the Federal Government's opposition to worldwide combined reporting as applied to U.S.-based taxpayers is based solely on issues of tax policy, not foreign policy, and therefore Colgate's Foreign Commerce Clause argument fails. SG Br. 26-27. The presumption behind the Solicitor General's argument is that tax policy necessarily is concerned only with domestic issues. This Court's Foreign Commerce Clause jurisprudence, however, does not turn on mere semantics (that is, whether the Federal Government uses the phrase "tax policy" as opposed to "foreign policy") but rather analyzes the concerns underlying the Federal Government's position. As demonstrated in Colgate's opening brief, there is no question that the Federal Government's opposition to California's taxing method as applied to U.S.-based taxpayers was founded upon concerns relating

to that taxing method's impact upon the nation's foreign commercial and economic policy. *See* Pet. Br. 40-42.[16]

CONCLUSION

For the reasons set forth in our opening brief and in this reply brief, the judgment of the California Court of Appeal should be reversed.

Respectfully submitted,

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[16] Indeed, the Solicitor General's position is contradicted by evidence that he himself presents. In 1982, the United States filed a brief *amicus curiae* in *Chicago Bridge*, a case involving the imposition of worldwide combined reporting on a domestic-based taxpayer. The tax years at issue in *Chicago Bridge* were 1969-74 and therefore overlap the years at issue in this case. According to the Solicitor General himself, not only were "the government's criticisms of the worldwide method . . . couched in constitutional terms" but also "the government's opposition . . . extended to cover the method's application to domestic corporations with foreign subsidiaries." SG Br. 8. This admission by the Solicitor General clearly contradicts his own assertion that while "the executive branch since 1982 has opposed the State's application of WWCR to domestic as well as foreign corporations" (SG Br. 26), that opposition has "not asserted . . . that application of WWCR to domestic taxpayers interferes with the federal government's conduct of foreign relations." *Id.*

APPENDIX A

Extract from Transcript of Oral Argument Before the Court of Appeal

MR. SCHELL: Your honor, I would like to either by subsequent written request or oral request that the court take judicial notice of the State of California's Controller's Financial . . . General Purpose Financial Statements for the 1989-90 fiscal year, in which the Controller gives an estimate of the tax impact of this case with respect to the prospectivity argument, that tax impact . . .

P.J. PUGLIA: What possible effect could that have upon our decision?

MR. SCHELL: Just with respect to the *James B. Beam* retroactive/prospective argument, the equities, it . . . the tax impact is stated in the Controller's report . . .

MR. KLEIER: And if we can state our objections. This issue was obviously not before the trial court, and it is too late to present the issue for the first time on appeal, particularly because it would require findings of fact on the hardship issue. But to raise that issue . . .

P.J. PUGLIA: I think counsel is correct.